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April 14, 2010

Jennifer J. Johnson
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, D.C. 20551

Re: Docket No. R-1384, Truth In Lending Act, Regulation Z

Dear Ms. Johnson:

GE Money Bank appreciates the opportunity to comment on the most recent round of proposed regulations scheduled to take effect on August 22, 2010. 75 Fed. Reg. 12334 (Mar. 15, 2010). GE Money Bank is a federal savings bank located in Utah. As a major private label and co-brand credit card issuer, GE Money Bank partners with over 100 retail brands and more than 100,000 small business merchants to provide over 100 million consumers with private label and co-brand credit card accounts.

The availability of store credit, including credit provided by GE Money Bank as part of our private label and co-brand programs, is a critical driver of the economy (especially retail sales) because it provides increased purchasing power to consumers. Consumers also have special affinity with our retail partners and receive valuable discounts and promotions in connection with the use of private label and co-brand cards, saving consumers a significant amount of money every year.

Background

Our programs, which we operate in conjunction with our retail clients, are designed to enhance and reward customer loyalty, provide a variety of customer benefits and discounts and increase retail sales. A very significant portion of the sales of our major retail clients are made on our credit cards. In fact, we have clients who routinely have 25% to 40% of their sales on our private label card, and there have been instances where a client of ours has experienced penetration rates (percentage of sales on our card of total retailer sales) of over 70% on specific days when cardholder credit events are running.

Retail customers who hold private label cards are more loyal to the co-sponsoring retailer than other customers and often benefit from discounts, rewards and other special offers from retailers that are not available to the general public. In many cases, our retail partners have an interest in the economics of the credit program to help fund these rewards and discounts to their best customers. Late payment fees (as well as APRs) are key components of the economic equation that enables these programs to deliver value to customers.

"Reasonable and Proportional" Penalty Fees

The Board has determined that the reasonableness of penalty fees should be judged on the basis of a cost analysis, a deterrence analysis or compliance with a safe harbor. We agree that using cost, deterrence and a safe harbor to determine reasonableness makes sense and strongly recommend retaining all three methods in the final regulation given the variety of different credit programs and card issuers to which the rule will apply. However, we urge the Board to incorporate the points below into the final rule.

Cost

The introductory explanation accompanying the proposed regulation reflects the Board's understanding that "as a general matter, card issuers currently do not price for the risk of loss through penalty fees" 49 Fed. Reg. at 12341. It cites the UK Office of Fair Trading's statement of credit card principles, stating: "if card issuers were permitted to begin recovering losses and associated costs through penalty fees rather than upfront rates — transparency in credit card pricing would be reduced." The Board solicits comment on whether losses and associated costs should be included in the cost analysis for purposes of determining reasonableness.

We respectfully must disagree with the Board's general assumption that card issuers do not price for the risk of loss through penalty fees. In fact, issuers do rely on penalty fees to manage the risk of loss during the on-going account relationship. Credit card issuers can price for risk when the APR is initially set on the account. However, late fees provide card issuers with an efficient and targeted way to charge more to consumers who demonstrate higher risk on that account through late payments and to avoid the undesirable consequence of requiring less risky consumers who pay on time to subsidize late payers. Card issuers are permitted to increase APRs on future transactions if a consumer pays late, but the ability to offset risk through such increases is very limited for a variety of reasons, including uncertainty whether additional credit will be extended. Moreover, even if some card issuers currently do not price for risk of loss through penalty fees, nothing in the Credit CARD Act would prevent them from doing so in the future and the Board's regulations should not impose such a limitation.

Additionally, charging those fees to customers who do not comply with the credit agreement enables us to approve credit for certain credit segments who may not otherwise generate enough revenue to offset their risk. Reducing late payment fees would prevent us from offering those accounts and result in lower credit availability among customer segments that need it most. Theoretically, we could increase the APRs charged to all consumers, including those who pay on time, to subsidize the costs that should be paid by late payers. This would have the undesirable effects of shifting cost from transactors to revolvers (because only revolvers pay periodic interest) and from late payers to responsible payers.

We also disagree that late payment fees are not "transparent." Late payment fees are prominently disclosed in solicitations, account opening documents and now on every billing statement. Due to the regulatory changes that took effect last August and in February 2010, customers now have every opportunity to pay on time. Their payment due date is fixed, they have at least 21 days to pay and every statement includes a late payment warning disclosing the amount of the possible late payment fee. In addition, assessing late payment fees against customers who do not comply with their terms is more fair than assessing higher APRs on all customers, even those who pay on time.

Further, we believe that there are significant differences between credit card regulation in the U.K. and the U.S. that must be recognized in evaluating whether the approach to penalty fees in that country is appropriate in the U.S. Regulation Z, as recently amended, essentially eliminates the ability of credit card issuers to price for risk through APR increases on existing balances. However, in the U.K., card issuers are not subject to general limitations on increasing rates on outstanding account balances. It would be unfair to subject U.S. card issuers to the same limits on late fees as U.K. issuers when U.K. issuers have this additional ability to price for portfolio risk through APR increases on existing balances. Moreover, U.S. credit card regulations implicitly allow higher late fees by permitting such fees to be used as a penalty, while penalty pricing is generally not allowed in the U.K.

We understand that there is some debate about whether late payment fees are always avoidable. While reasonable minds could differ as to whether customers with specific hardships (*e.g.*, unexpected medical expenses) could avoid late payment fees, we and other issuers have specific hardship programs to address those exceptions. Accordingly, we believe a cost justification should be permitted to include credit losses and reserves — and that if the Board is concerned about unavoidable situations, it could make an exception for losses and reserves with respect to hardship accounts and disallow only that portion of total losses and reserves.

We disagree with the Board's view that losses should be excluded entirely from the cost consideration because there is not a sufficient correlation between late payers and losses. The Board apparently bases this conclusion on its belief that a particular percentage of consumers who pay late twice (estimated by the Board to be 93% (see fn. 17 at 75 Fed. Reg. 12341)) never charge off. We respectfully submit that the relevant consideration is the difference between the charge off rates of late payers and consumers who pay on time, rather than the absolute charge off rates for late payers. If late payers are x% more likely to charge off than timely payers, then a proportionate share of the losses and reserves caused by late payers should be borne by the late payers. Such an allocation is undeniably more fair than allocating such losses and reserves among consumers who pay on time. We believe that it is indisputable that late payers cause more losses and reserves and, thus, that it is inappropriate to exclude losses entirely from the cost calculation.

Finally, even if card issuers are not able to produce an adequate analysis of the connection between losses and late payers in the extremely constricted time period of this

rule making, the Board's rules should leave open the possibility that losses can be considered by a particular card issuer if that card issuer can demonstrate a requisite connection in the future. Stated differently, losses undoubtedly are costs associated with late payers and any statistical difficulties in measuring the correlation and proportionality of those costs with particular late payment data should be addressed over time by applying the appropriate statistical analysis to the relevant data that is available from time to time, and not by categorically excluding the possibility of considering losses with an appropriate statistical basis.

Finally, we think it is important to recall that Congress directed that penalty fees be reasonable and proportional to the terms violation. Card issuers should be able to satisfy this standard through objective data that is reasonably verifiable. We do not believe that Congress intended, or that it would be good policy, to require card issuers to engage in elaborate cost accounting that is subject to extraordinary uncertainty and expense. We believe that the Board should allow card issuers to consider general industry data, with appropriate adjustments to account for special circumstances, in establishing that the amount of its fees are reasonable and proportional.

For these reasons, we strongly encourage the Board to adjust the regulation relating to cost justification so as to allow credit losses and credit costs to be included as part of the late payment fee justification, and in the other ways described above.

We also strongly urge the Board to make clear that card issuers can consider the collectability of late fees in setting the fee amount under the cost analysis. We agree with the Board that Congress intended to "permit[] card issuers to use penalty fees to pass along the costs incurred as a result of violations . . ." 49 Fed. Reg. at 12339. Since a card issuer collects less than 100% of the late fees it imposes, it will not be reimbursed for the costs incurred as a result of violations unless it can allocate those costs among the individuals that actually pay late payment fees; otherwise, the issuer must bear the cost of violations to the extent that net late fees received is less than gross fees charged.

Deterrence

We applaud the Board for recognizing the critical importance of meaningful late payment fees in deterring late payments. We agree that customers must have an appropriate financial incentive to pay on time and that such an incentive is important to holding credit losses in check and operating a safe and sound loan program. We believe that reducing late payment fees will result in higher losses. Our own experience shows that as late payment fees have increased, entry rates (which are the percentage of accounts moving to 30 days past due) have dropped — even during the worst recession since the Great Depression.

We understand the Board's interest in providing for a fair model to determine deterrence, but we believe that the Board's proposal on deterrence has very serious problems and may effectively prevent card issuers from using it. Congress expressly determined that deterrence is an appropriate purpose for penalty fees and we believe

strongly that the Board's rule should provide a reasonable and workable framework to carry out that determination.

To start with, we respectfully submit that the test in the proposal needs to be revised to provide reasonable guidance of the standard that the Board is intending to set. The Board has indicated that the issuer would need to show statistically that the imposition of a lower fee would result in a substantial increase in the frequency of violation. This formulation considers only the relative deterrent effect of different fee amounts, and provides no guidance on the primary issue of the appropriate level of deterrence. Absent guidance on the appropriate level of deterrence, the standard is likely to be unworkable and may lead to unintended or undesired results.

Second, apart from uncertainty regarding the applicable test that needs to be met, we are concerned that the Board's proposal imposes administrative obstacles that may be insurmountable for most if not all credit card issuers, and thus prevent issuers from using this option. Virtually no card issuer will have the data to conduct a statistical analysis of the deterrent effect of various late fee amounts because issuers generally impose relatively uniform late fee amounts on their portfolios and, given the extraordinarily short time period for rule making on penalty fee limits, issuers do not have time to test fee amounts before the effective date of the new rule. One possible way to allow card issuers to be able to collect such data would be to have a safe harbor amount that is relatively high for a period (e.g. one year) that would allow card issuers to collect data to verify the deterrent impact of late fees at various amounts. Alternatively, the Board might allow issuers to charge fees of varying amounts after the effective date of the rule to the extent necessary under reasonable business practices to test and validate the impact of different fee amounts on deterrence. Because we do not have time to conduct our deterrent fee testing before the August 22, 2010 effective date, we effectively may be precluded from doing so unless special flexibility for testing is provided after the regulation becomes effective.

We further think that the requirement of an "empirically derived, demonstrably sound" statistical model is not appropriate for the deterrent analysis. This concept obviously is borrowed from the Board's Regulation B in the context of being able to consider age in connection with a credit scoring system. However, scoring systems (as opposed to judgmental systems) are by their nature mathematical models. Here, card issuers do not statistically model the deterrent impact of late fees and the Board's proposal creates an unreasonably difficult obstacle to considering the legitimate need for a late fee to serve as deterrent. More generally, as noted above, we think that a test of "reasonable and proportional" should not require statistical proof that will be extraordinarily expensive and time consuming, and provide little if any benefit to consumers.

We believe that the Board should permit card issuers to use deterrence considerations in setting the late fee amount as long as they have objective and reasonably verifiable bases for concluding that the fee meets the relevant test. The Board also should expressly provide card issuers flexibility to consider various sources of

objective and reliable information in assessing such deterrence, including our own experience and general industry information. It is not reasonable for the Board to believe that the deterrent effects of fee amounts are going to vary so substantially between individual card issuers to justify the cost in time and money for each issuer to conduct its own individual statistical analysis to set the fee in the first instance, and then to validate it on a regular basis. There is simply no reason for the Board's regulation to require an excessively elaborate process akin to a utility rate-making that will benefit only lawyers, accountants and statistical consultants. Indeed, Congress merely imposed a general standard of "reasonable and proportional" and not mathematical or statistical certainty.

We also believe that the Board should expressly provide card issuers with flexibility in employing reasonable methods of measuring deterrence, including through consideration of loss metrics, even if the amount of the late fee cannot be statistically isolated. For example, if as a result of reducing late fees to comply with these regulations, a card issuer experiences an increase in credit loss metrics (e.g., percentage of accounts missing payment due dates, percentage not paying by the end of the billing cycle, percent charging off, severity of loss, etc.), the issuer should be permitted to increase late payment fees to stabilize such loss measures and avoid incremental credit losses. This actual experience should be sufficient to demonstrate the requisite correlation between credit costs, deterrence and late fee amount. It would be unfortunate if by complying with the rules, the issuer simply had to live with an increased loss rate indefinitely without any realistic way to address the situation because of limits in statistical analysis and difficulties with the Board's test.

In sum, we believe the Board should substantially revise the provisions of the rule on deterrence substantially or it will be extraordinarily difficult, if not impossible, for card issuers to take deterrence into account in setting fees. Such a result is unfair to card issuers and inconsistent with Congressional intent to impose reasonable limits on penalty fees – Congress surely did not intend that issuers be precluded from charging reasonable late fees because of a standard that is inherently unworkable.

Safe Harbor

We also applaud the Board for recognizing the need for a safe harbor as an alternative to cost- and deterrence-based justifications of penalty fees. We strongly believe that if late payment fees otherwise have to be justified by a cost or deterrence analysis, a safe harbor is very important to enable issuers to avoid gray areas and challenges.

The safe harbors will be extremely important to the institutions that do not want to (or are unable to) invest in substantial and costly undertakings to assess cost and deterrent effects. Given the manner in which the Board has proposed the cost and deterrence options, many card issuers (both large and small) can be expected to be unable to take advantage of them. Although Congress intended to impose reasonable limits on penalty fees, it did not intend to prohibit them implicitly through application of unworkable standards or requirements.

We strongly support a dollar amount minimum for the safe harbor on late fees. Many of our minimum payment amounts are relatively low, for example between $25 and $50. If the safe harbor is merely 5% of the minimum payment amount, the late fee would be only between $1.25 and $2.50. Such de minimis late fee amounts clearly would have virtually no deterrent effect on consumers who otherwise might pay late. Such late fee amounts also would require extraordinary increases in APRs to maintain current revenues (with resulting excessive subsidization of late payers) or dramatic decreases in the availability of credit.

We ask that the safe harbor be set high enough to realistically deter customers from paying late, and to allow card issuers to recover the costs incurred by late payers (through net fees paid). The practical limits noted above with the individual assessment options may well limit the ability of card issuers to set appropriate fee amounts on their own. Setting the late payment fee safe harbor too low would have the following undesirable consequences:

- Credit program revenue would decrease, resulting in a need to further increase APRs or other fees, and/or to decrease credit card benefits and rewards that our customers value.

- Certain credit segments may no longer qualify for credit and credit availability will shrink — this will hurt retail sales as well as the customers who need, but cannot get, credit.

- Private label credit will be disproportionately affected versus general purpose credit because private label credit does not have interchange as a component of the revenue equation and fee revenue represents a proportionately higher percentage of total account revenue.

We also suggest that the Board provide card issuers the flexibility to determine different late fee amounts as long as the average late fee amounts are lower than the safe harbor set by Board. The requirement that the average late fee amount be lower than a specified amount will ensure that the late fees generally meet the reasonable and proportional requirement. Moreover, the ability to tier late fees within that limitation will provide card issuers the ability to develop fee amounts that accomplish the Congressional goals of allowing the recovery of costs and deterring late payments.

Proportionality

The Board has also proposed a general rule that a penalty fee should not exceed the "amount of the violation" and that for late payments, the amount of the violation is the unpaid portion of the missed minimum payment.

We believe that the "amount of the violation" should not be the unpaid portion of the missed payment; rather, it should be the full amount of the minimum payment. Limiting

the amount of late fees to the amount that a scheduled payment is short would be inconsistent with both the cost and deterrent purposes of the rule. It is likely to cost the same amount for issuers to send letters and make calls when a minimum payment is not made, whether the shortfall is large or small. Similarly, the fee amount is intended to be a deterrent to not making the minimum payment. Setting the fee amount in relation to only the shortfall effectively allows the consumer to decide the deterrent effect of the payment by deciding the portion of the payment that they will make. Moreover, although many card issuers adjust late fee amounts based on account balance or scheduled minimum payments, we believe that card issuers will incur significant operational costs if they are required to modify systems to determine the late fee amount based on the shortfall between the actual and scheduled payment. Finally, focusing only on the shortfall in the minimum payment is not appropriate because when a late payment arguably puts repayment of the entire balance at risk, since portfolio performance demonstrates a direct correlation between higher loss rates and late payments.

We also request that the Board create an exception to the "amount of the violation" requirement for minimum payments below a specified amount (*e.g.* $25). The proportionality requirement does not require a linear relationship between the amount of the violation and the fee. The Board has recognized the need for a minimum fee amount in the proposal on the safe harbor, and the need for the fee to serve as a deterrent compels the same result with respect to the proportionality requirement. Currently, many card issuers offer accounts on which the minimum payment may be $20 or $25. Assuming that the safe harbor minimum late fee is $30, applying the proportionality rule to low minimum payments would prevent card issuers from using the fee for its legitimate deterrent effect.

Late Fee Warning Disclosure

We commend the Board for recognizing the adjustments to the late fee warning disclosures on periodic statements that are needed because of the limits on late fees in the proposal. However, we request that the Board expressly confirm in the Commentary that the warning message on statements need only state the highest late payment fee that could be charged under the terms of the cardholder agreement, and that it is not necessary for issuers to vary the message based on circumstances that may change from month to month or between cardholders. For example, if the cardholder agreement provided for a maximum late payment fee of $30 in accordance with the safe harbor provision, the account balance was $100 and the minimum payment owed was $15, the issuer should be allowed to include the $30 figure in the late payment warning message even if the issuer is limited to charging $15 in that particular month. Requiring the late payment message to be tailored to reflect the lesser of the late payment fee in the cardholder agreement and the highest late payment fee for a particular month or accountholder would be very burdensome, as well as unnecessary from a customer disclosure perspective.

Reevaluation of Changes In Terms

The Board has proposed rules to implement the Credit CARD Act provision that changes in terms since January 1, 2009 be reevaluated periodically. We believe the Board's approach in allowing the issuer to use the factors used originally in changing the rate, or the factors used to establish rates for new accounts, makes practical sense, although as noted below we also think some clarifications are needed to make the approach workable.

To start with, the Board has asked for guidance as to how long the reevaluation should apply to an account. Our view is that the reevaluation should continue until the earlier of: (i) the date the account is at the same pricing offered to new accounts with comparable risk profiles in the same program or portfolio, or (ii) the date two years after the relevant change in terms to the account. We believe that if the customer is being priced like other new customers there is no further need for review, and requiring additional review every six months would be an unnecessary compliance burden. Of course, if the customer's pricing were changed again, a new reevaluation cycle would start.

We also believe that the reevaluation requirement should not apply to accounts that are moved into delinquency pricing for prospective purchases based upon a contractual trigger if those accounts already receive the benefit of a cure after a specified number of on-time payments. In addition, we do not believe that the reevaluation requirement should apply to APR increases from a promotional rate to a standard rate at early termination in accordance with the promotional terms (the rule already would not require reevaluation of a promotional rate that expires naturally because no change in terms notice is required for such expirations). A promotional rate is by its very nature temporary and more favorable than the standard rate, and its termination (as permitted by the terms of the promotional offer and Regulation Z) is agreed upon by the parties when the consumer enters into transaction. This exception is especially important for promotional transactions entered into after January 1, 2009 (because APR increases after that date generally must be reevaluated) and before February 22, 2010 (when the general prohibition on rate increases went into effect).

We also request that the Board confirm that a private label card issuer with multiple card portfolios can comply with the reevaluation requirements based on the terms and conditions of each portfolio independently. For example, if the current rates on the portfolio are X% for Merchant A and Y% for Merchant B, the X% rate would be used for reevaluating rate increases for Merchant A accounts and the Y% would be used for reevaluating rate increase for Merchant B portfolio. This is necessary because the economics of portfolios for different merchants can vary significantly.

In addition, we ask that the Commentary expressly provide that a card issuer that is applying pricing standards for new accounts in reevaluating APR increases on existing accounts be able to make appropriate adjustments to those standards to reflect that they are being applied to an existing account and not a new applicant. For example, card

issuers should be able to take into account an existing cardholder's payment and performance history on the existing account when reevaluating the APR even though the issuer is not able to consider such data when evaluating an application for a new account.

We also submit that a period of 30 days is insufficient to implement an APR decrease after reevaluation. Because of operational problems with imposing multiple periodic rates in a single billing cycle, rate increases generally can be implemented only at the beginning of a billing cycle. If an account cycles shortly after the reevaluation process is completed, there will not be sufficient time to implement the APR decrease before the next cycle begins and the issuer will be required to wait until the beginning of the next billing cycle. Thus, we believe a 60-day time period is needed.

Transition Rules

In addition to our comment on the substantive rules, we have one transition rule request. Because we offer credit at the point of sale, we are very concerned about the timeline involved in changing out our credit applications in time for the August 22 implementation deadline, especially since we will have just changed out the point of sale in time for the July 1 compliance date on new Schumer box and other requirements. Additionally, given the fact that the proposed rules came out behind schedule, it will not be possible for us to replace all applications again to reflect the penalty fee changes between the time the final rules are promulgated and August 22. For this reason, we ask that we be given a transition period after the final regulations are promulgated to replace our credit applications to reflect the new late fee structure. During this time, we would not want to be considered non-compliant if our credit disclosures continued to reflect the old late fee structure, as long as we are not charging fees inconsistent with the new rules. The most workable transition rule would be to allow us to exhaust our existing supply of stock before we replace with disclosures at the lower fee amounts. If a time limit needs to be imposed, we request that it be at least 180 days from the effective date. We also note that this transition rule should apply whenever the late fee amounts are decreased, either as a result of changes in the safe harbor amounts, or the card issuer's individual assessment of the cost and deterrent factors.

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We appreciate the opportunity to comment and would be pleased to answer any question you may have.

Sincerely,

Kurt Grossheim

Kurt Grossheim
President
GE Money Bank